

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **201138018**
Release Date: 9/23/2011

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:

Index Number: 1295.02-02

, ID No.
Telephone Number:

Refer Reply To:
CC:INTL:B02
PLR-142901-10
Date:
June 15, 2011

Re:

LEGEND:

Shareholder =

PFIC =

State =

Products =

Entity A =

Entity B =

Entity C =

Entity D =

Entity E =

H =

J =

K =

Location 1 =

Location 2 =

a% =

b% =

c% =

d% =

e% =

f% =

g% =

h% =

j% =

k% =

Date 1 =
Date 2 =
Date 3 =
Date 4 =
Date 5 =
Date 6 =
Date 7 =
Date 8 =
Date 9 =
Year 1 =
Year 2 =
Year 3 =
Year 4 =
Amount 1 =
Amount 2 =
Amount 3 =
Amount 4 =
Amount 5 =
Amount 6 =
Amount 7 =
Amount 8 =
Amount 9 =
Amount 10 =
Amount 11 =
Amount 12 =
Amount 13 =
Amount 14 =
P =
Q =
R =
S =
T =
U =
Current GTC =
University =

W =
X =
ITM =

Dear :

This is in response to a letter dated October 12, 2010, submitted by
Shareholder's authorized representative, requesting the consent of the Commissioner of

the Internal Revenue Service (IRS) for Shareholder to make a retroactive qualified electing fund (QEF) election under section 1295(b) of the Internal Revenue Code (Code) and Treas. Reg. § 1.1295-3(f) with respect to its indirect investment in PFIC.

The ruling contained in this letter is based upon information and representations submitted by Shareholder and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the material submitted in support of the request for a ruling. Verification of the factual information, representations, and other data submitted may be required as part of the examination process.

FACTS

Shareholder, a limited liability company formed under the laws of State and treated as a partnership for U.S. federal income tax purposes, is owned a% by Entity A and b% by Entity B. Shareholder began operations on Date 2. Through its U.S. and foreign subsidiaries and joint ventures, Shareholder manufactures and markets a wide range of Products, with manufacturing facilities located in several countries throughout the world. PFIC was formed on Date 5 and is an indirect subsidiary of Shareholder.

Shareholder directly owns c% of the voting membership interests in Entity C, a limited liability company formed under the laws of State on Date 1 and treated as a disregarded entity for U.S. federal income tax purposes. Entity C directly owns a d% voting interest in the shares of Entity D, formed on Date 4 and treated as a partnership for U.S. federal income tax purposes. The remaining e% ownership interest in the shares of Entity D is owned by Entity E (which is unrelated to Shareholder).

Entity D directly owns an f% voting interest in the shares of PFIC. The remaining g% interest in the shares of PFIC is owned by entities unrelated to Shareholder. Therefore, Shareholder indirectly owns an h% (d% of f%) equity interest in PFIC.

One of Shareholder's significant foreign joint venture projects is the construction and operation of H, located in Location 1 and owned by Entity D (the Entity D Project). As part of the Entity D Project, a J was constructed in Location 2 (the PFIC Project). The principal objective of the PFIC Project is to K. The PFIC Project is owned by PFIC and began commercial operations in Date 9.

To finance the construction of the PFIC Project, Entity D funded its portion of the project construction costs through shareholder advances. From time to time, the amount of shareholder advances received by PFIC exceeded the amount immediately required by PFIC to pay construction costs, and such excess amounts were placed on deposit with overseas banks. Beginning in Year 2, interest on these deposits generated the passive income that gave rise to PFIC's passive foreign investment company status.

In its audited financial statements for Year 2 and Year 3, PFIC reported on its Statement of Comprehensive Income as “other income” amounts that Shareholder now knows to be interest income (*i.e.*, passive income within the meaning of Code section 1297(b)). PFIC first reported its “other income” specifically as “finance income” in its Year 4 audited financial statements. The total amount of interest income earned by PFIC for the tax Years 2 through 4 was Amount 1, and Shareholder’s pro rata share of such income was Amount 2. The amount of interest income reported by PFIC in its audited financial statements was immaterial to PFIC (or to Shareholder’s pro rata share thereof) in any given year, or in the aggregate, relative to the portion of PFIC’s general and administrative expenses (G&A Expenses) and capital expenditures (CapEx) reported by PFIC in its annual audited financial statements. PFIC’s G&A Expenses were Amount 3 in Year 2, Amount 4 in Year 3, and Amount 5 in Year 4. PFIC’s CapEx were Amount 6 in Year 2, Amount 7 in Year 3, and Amount 8 in Year 4. PFIC’s “other income” or “finance income” was Amount 9, Amount 10, and Amount 11 (and Shareholder’s pro rata share of such income was Amount 12, Amount 13, and Amount 14) for Years 2 through 4, respectively. As reported from Year 1 through Year 4, PFIC’s aggregate “other income” or “finance income” amounts represented j% of its G&A Expenses and k% of its cumulative CapEx. As a result, PFIC reported losses in each of Years 1 through 4.

Since its inception on Date 2, Shareholder has maintained an in-house tax department, staffed with qualified and experienced tax professionals, each charged with providing Shareholder sound and reliable U.S. international tax planning and compliance for its worldwide operations. The level of staffing has fluctuated between P and Q tax professionals, including (a) the General Tax Counsel (GTC), (b) R to S tax attorneys and (c) T to U tax accountants and tax analysts.

Shareholder’s board of directors appoints the officers of Shareholder, including the GTC, who manages the day-to-day activities and affairs of Shareholder’s in-house tax department. The GTC also reports to an Advisory Tax Committee made up of two members each from Entity A and Entity B.

The GTC’s duties include the management and oversight of: (1) the tax attorneys providing tax counseling and advice with respect to structuring Shareholder’s overseas expansion projects (including the Entity D and PFIC Projects); (2) the tax attorneys negotiating tax provisions of joint venture and other agreements associated with Shareholder’s overseas expansion projects, and (3) the U.S. tax compliance responsibilities of Shareholder’s international tax compliance function.

Shareholder has had two GTCs since its inception. The former GTC held office from Date 2 until Date 6, and the Current GTC was appointed in Date 7. Prior to beginning employment at Shareholder, the former GTC had obtained extensive tax experience working primarily in industry in various tax counseling and tax compliance roles. In Date 6, the former GTC resigned his position with Shareholder. Between

Dates 6 and 7, the role of GTC was vacant and was in effect carried out through the joint efforts of two of Shareholder's then more senior tax attorneys.

Effective Date 7, Current GTC was appointed by Shareholder. Prior to his current role, Current GTC was a lecturer with University, where he taught various tax and accounting classes. Prior to his tenure at University, Current GTC spent W years with a predecessor to Entity B serving in various tax counseling roles.

Shareholder has had one manager of its international tax compliance function, the International Tax Manager (ITM), since its inception. He was hired effective Date 3. Prior to joining Shareholder, the ITM spent X years in various financial accounting and tax compliance positions with Entity A. The ITM's duties with Shareholder include filing all U.S. tax and information returns related to Shareholder's international operations. From its inception until Date 8, Shareholder also employed a Tax Compliance Manager (TCM), to whom the ITM directly reported. The role of TCM has been vacant since Date 8. In addition, since its formation, Shareholder has had four different tax attorneys charged with responsibility (at different times) for providing tax counseling and planning for Shareholder's international operations, including tax planning and advice on the negotiation and implementation of the Entity D and PFIC Projects.

By the time PFIC was formed, Shareholder had already embarked on a highly capital-intensive expansion of its foreign operations. However, prior to Date 7, the ITM was not directly involved in Shareholder's foreign expansion projects, relying instead on the tax attorneys charged with providing tax counseling and planning on those projects for information on the tax aspects of those projects. The ITM's direct role in such projects has steadily grown since then.

Notwithstanding the considerable tax resources allocated to Shareholder's overseas expansion strategy, Shareholder failed to (a) timely file a check-the-box election to treat PFIC as a partnership for U.S. federal income tax purposes (as contemplated in PFIC's joint venture agreement), resulting in the classification of PFIC as a corporation for U.S. federal income tax purposes, and (b) subsequently identify that PFIC could be a passive foreign investment company in Year 2, when PFIC first began to earn passive income. Factors contributing to these failures included the reporting by PFIC of its interest income as "other income," the resignation of the former GTC, the period of time that the GTC position was vacant, and the transition of the Current GTC into his role. In short, the tax professionals in Shareholder's in-house tax department failed to recognize that PFIC began to earn passive income and, as a result of that unintended oversight, Shareholder reasonably believed that PFIC had not become a passive foreign investment company. At no time prior to Date 9 did Shareholder's tax professionals inform Shareholder of its need to make a QEF election for PFIC, nor of the tax ramifications of failing to make such an election.

Shareholder's Current GTC and ITM have submitted affidavits, under penalties of perjury, describing the events that led to the failure to make the QEF election by the election due date, including the role of Shareholder's in-house tax professionals. Shareholder represents that, as of the submission date of its request, the passive foreign investment company status of PFIC had not been raised by the IRS on audit for any taxable year of Shareholder.

RULING REQUESTED

Shareholder requests the consent of the Commissioner to make a retroactive QEF election under section 1295(b) of the Code and Treas. Reg. § 1.1295-3(f) to treat PFIC as a QEF with respect to Shareholder for all taxable years starting in Year 2.

LAW

Section 1295(a) provides that any passive foreign investment company shall be treated as a QEF with respect to a taxpayer if (1) an election by the taxpayer under section 1295(b) applies to such company for the taxable year, and (2) the company complies with such requirements as the Secretary may prescribe for purposes of determining the ordinary earnings and net capital gains of such company.

Under section 1295(b)(2), a QEF election may be made for any taxable year at any time on or before the due date (determined with regard to extensions) for filing the return for such taxable year. To the extent provided in regulations, such an election may be made after such due date if the taxpayer failed to make a timely election because the taxpayer reasonably believed that the company was not a passive foreign investment company.

Under Treas. Reg. § 1.1295-3(f), a shareholder may request the consent of the Commissioner to make a retroactive QEF election for a taxable year if:

1. the shareholder reasonably relied on a qualified tax professional (including a tax professional employed by the shareholder), within the meaning of Treas. Reg. § 1.1295-3(f)(2);
2. granting consent will not prejudice the interests of the U.S. government, as provided in Treas. Reg. § 1.1295-3(f)(3);
3. the request is made before a representative of the IRS raises upon audit the passive foreign investment company status of the corporation for any taxable year of the shareholder; and
4. the shareholder satisfies the procedural requirements of Treas. Reg. § 1.1295-3(f)(4).

The procedural requirements of Treas. Reg. § 1.1295-3(f)(4) include filing a request for consent to make a retroactive election with, and submitting a user fee to, the

Office of the Associate Chief Counsel (International). Treas. Reg. § 1.1295-3(f)(4)(i). Additionally, affidavits signed under penalties of perjury must be submitted describing:

1. the events which led to the failure to make a QEF election by the election due date;
2. the discovery of such failure;
3. the engagement and responsibilities of the qualified tax professional; and
4. the extent to which the shareholder relied on such professional.

Treas. Reg. §§ 1.1295-3(f)(4)(ii) and (iii).

CONCLUSION

Based on the information submitted and representations made, we conclude that Shareholder has satisfied Treas. Reg. § 1.1295-3(f). Accordingly, consent is granted to Shareholder to make a retroactive QEF election with respect to Shareholder's indirect investment in PFIC for Year 2, provided that Shareholder complies with the rules under Treas. Reg. § 1.1295-3(g) regarding the time and manner for making the retroactive QEF election.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

A copy of this ruling must be attached to any tax or information return to which it is relevant.

In accordance with the Power of Attorney on file with this office, copies of this letter are being sent to your authorized representatives.

Sincerely,

Jeffery G. Mitchell
Chief, Branch 2
Office of the Associate Chief Counsel
(International)

cc: